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ESSAY

PATENT EXHAUSTION AND FEDERALISM: A HISTORICAL NOTE

*Herbert Hovenkamp**

PROFESSORS Duffy and Hynes offer an interesting, patent-centric interpretation of the first sale (exhaustion) doctrine in patent law, arguing that the doctrine’s principal purpose is to constrain the scope of patent law in order to avoid displacing nonpatent law.¹ I am not entirely persuaded. Sometimes the doctrine seemed to do just the opposite, depending on which way the wind was blowing. For example, exhaustion doctrine accommodated antitrust quite well during periods of antitrust expansion, serving the purpose that Duffy and Hynes describe. As antitrust law went in the other direction, however, exhaustion doctrine often led courts to find practices such as tying, exclusive dealing, or resale price maintenance (“RPM”) to be procompetitive, and exhaustion doctrine went right on refusing to enforce such agreements through infringement suits. As a result, exhaustion doctrine served to blockade rather than facilitate state and federal competition law. To the extent that doctrinal change allowing patent doctrine to reach beyond those in privity of contract was socially valuable, the first sale doctrine impeded rather than accommodated that change.² To be sure, unwavering doctrinal stability

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¹ John F. Duffy & Richard Hynes, Statutory Domain and the Commercial Law of Intellectual Property, 102 Va. L. Rev. 1 (2016).

² See Herbert Hovenkamp, Post-Sale Restraints and Competitive Harm: The First Sale Doctrine in Perspective, 66 N.Y.U. Ann. Surv. Am. L. 487, 524 (2011). The principal rele-

in one area of law will generally force other areas to invent around it in order to reach defensible results, but that is less a defense of Duffy and Hynes's position than a simple historical explanation.

Nevertheless, as a historical explanation there is much to be said for Duffy and Hynes's argument. Here, I propose a modest historical revision. During its heyday in the late nineteenth and early twentieth centuries, exhaustion doctrine developed as a creature of federalism, preserving the boundary between patent law, which by that time had become more or less exclusively federal, and state law respecting post-issuance patent use. The federalism issue was critical. Congress could amend or even eliminate judge-made patent law, but the Supremacy Clause³ required the states, including state antitrust law, to yield to federal patent policy.

Federal patent exclusivity had not always been a foregone conclusion. The Intellectual Property Clause grants Congress the power to grant patents but does not deny that power to the states.⁴ Some states continued to grant patents after the Constitution was ratified, and influential commentators such as Justice Joseph Story and Chancellor James Kent believed that the states had concurrent patent-granting authority.⁵ In *Gibbons v. Ogden*, the Supreme Court struck down a state-issued patent under the Commerce Clause but refused to determine "the right of the States to grant patents."⁶ By the middle of the nineteenth century, when the early exhaustion cases came down, state patents had largely disappeared, undoubtedly because federal patenting was more valuable to inventors. State patents would not be expressly preempted, however, for another century.⁷

Albert Henry Walker, writing in the fourth edition of his influential patent law treatise in 1904, observed that:

The reason why a State may regulate the sale of the patented thing, and may not regulate the sale of the patent covering that thing, is ex-

vance of privity of contract is that under the first sale doctrine, purely contractual restraints can continue to be enforced, but only against those who are in privity of contract. *Id.*; see Duffy & Hynes, *supra* note 1, at 5–6.

³ U.S. Const. art. VI, cl. 2.

⁴ *Id.* art. I, § 8, cl. 8.

⁵ See Herbert Hovenkamp, *The Emergence of Classical American Patent Law*, 58 *Ariz. L. Rev.* (forthcoming 2016).

⁶ 22 U.S. (9 Wheat.) 1, 239 (1824).

⁷ See *Compco Corp. v. Day-Brite Lighting, Inc.*, 376 U.S. 234, 237 (1964); *Sears, Roebuck & Co. v. Stiffel Co.*, 376 U.S. 225, 230–31 (1964).

plainable as follows. A patentee has two kinds of rights in his invention. He has a right to make, use, and sell specimens of the invented thing; and he has a right to prevent all other persons from doing either of those acts. The first of these rights is wholly independent of the patent laws; while the second exists by virtue of those laws alone. A patentee therefore holds the first of these rights subject to the police powers, and the taxing powers, of the State, and to the law regulating common carriers; while the second, being the creature of the laws of Congress, is wholly beyond State control or interference, by antitrust laws, or otherwise.⁸

Walker added the concluding reference to state antitrust law in the fourth edition.⁹

One characteristic of the patent system when Walker published the fourth edition of his treatise was intense federal oversight of the patent granting, construction, and enforcement process, but almost no oversight over how patents or patented articles were used subsequent to patent issuance. Where federal patent law stopped, state contract, commercial, and antitrust law kicked in. Thus, for example, the federal patent acts authorized licensing,¹⁰ but policing, interpreting, and enforcing the specific terms of license agreements were almost exclusively matters of state law.¹¹ That would change later in the twentieth century when the courts began to apply federal antitrust law to patent licensing practices.

One set of practices that threatened this state-federal balance post-sale was patent license restrictions enforceable by patent infringement suits. The reason is simple: Virtually any restriction that could be imposed by contract could also be imposed by a license restriction and be effectively “federalized,” because infringement suits were governed exclusively by federal law. For example, if a patentee imposed RPM, exclusive dealing, or tying restrictions on the sale plus license of a patented product, en-

⁸ Albert H. Walker, *Text-Book of the Patent Laws of the United States of America* 144 (4th ed. 1904).

⁹ Cf. Albert H. Walker, *Text-Book of the Patent Laws of the United States of America* 136 (3d ed. 1895) (not including concluding reference to state antitrust law).

¹⁰ 35 U.S.C. § 261 (2012). Such licensing was first authorized by Congress in 1952. See 35 U.S.C. § 261 (1952).

¹¹ See, e.g., *Keeler v. Standard Folding Bed Co.*, 157 U.S. 659, 666 (1895) (“Whether a patentee may protect himself and his assignees by special contracts brought home to the purchasers is not a question before us It is, however, obvious that such a question would arise as a question of contract, and not as one under the inherent meaning and effect of the patent laws.”).

forceable by an infringement action, then it would not matter whether state law prohibited the enforcement of such contracts. By turning the actions into ones of patent infringement (or contributory infringement), the patentee would effectively preempt state law.

Around the turn of the twentieth century, states first used their own antitrust laws to pursue practices such as tying,¹² exclusive dealing,¹³ and RPM.¹⁴ In most of these cases, condemnation under state law actually occurred before federal antitrust law even addressed the issue. Absent patent exhaustion, if these restraints were imposed via license restrictions and patent infringement suits, patent law would have preempted this state law. By contrast, federal antitrust law would apply whether or not there was a first sale.¹⁵ This explains why Congress reacted so quickly to the *Henry v. A.B. Dick Co.* decision, which had refused to apply patent exhaustion and then enforced a patent tie¹⁶—something that had already been condemned under state law.¹⁷ Within two years Con-

¹² See, e.g., *In re Op. of the Justices*, 81 N.E. 142, 145 (Mass. 1907) (upholding state law condemning patent ties).

¹³ See, e.g., *Butterick Publ'g Co. v. Fisher*, 89 N.E. 189, 190–91 (Mass. 1909) (applying state antitrust law to exclusive dealing); *Commonwealth v. Strauss*, 78 N.E. 136, 136 (Mass. 1906) (applying state antitrust law to exclusive dealing doctrine); *Tex. Brewing Co. v. Meyer*, 38 S.W. 263, 264 (Tex. 1896) (same).

¹⁴ See, e.g., *Klingel's Pharmacy v. Sharp & Dohme*, 64 A. 1029, 1029–30 (Md. 1906); *Brown v. Jacobs Pharmacy Co.*, 41 S.E. 553, 559 (Ga. 1902) (condemning resale price maintenance (“RPM”) nine years before the Supreme Court’s decision in *Dr. Miles Medical Co. v. John D. Park & Sons Co.*, 220 U.S. 373, 405 (1911), accomplished the same under federal law).

¹⁵ See, e.g., *Motion Picture Patents Co. v. Universal Film Mfg. Co.*, 243 U.S. 502, 516 (1917) (holding that both patent exhaustion and antitrust precluded enforcement of patent tie); *Straus v. Victor Talking Mach. Co.*, 243 U.S. 490, 501 (1917) (holding that patent exhaustion plus antitrust precluded enforcement of RPM clause contained in patent license); *Bauer & Cie v. O'Donnell*, 229 U.S. 1, 18 (1913) (similar); see also Ariel Katz et al., *The Interaction of Exhaustion and the General Law: A Reply to Duffy and Hynes*, 102 Va. L. Rev. Online 8, 13 (2016) (making a similar point).

¹⁶ 224 U.S. 1, 25, 49 (1912), overruled by *Motion Picture Patents Co.*, 243 U.S. at 518.

¹⁷ *In re Op. of the Justices*, 81 N.E. at 145, 147 (concluding that Massachusetts law could condemn patent ties). The court reached this conclusion after upholding from constitutional challenge a Massachusetts Senate bill, S. 275, 1907 Gen. Court, 128th Sess. (Mass. 1907):

Section 1. No person, firm, corporation or association shall insert in or make it a condition or provision of any sale or lease of any tool, implement, appliance or machinery that the purchaser or lessee thereof shall not buy, lease or use machinery, tools, implements or appliances or material or merchandise of any person, firm, corporation or association other than such vendor, or lessee, but this provision shall not impair the right, if any, of the vendor or lessor of any tool, implement, appliance or machine protected by a lawful patent right vested in such vendor or lessor to require by virtue of such patent right, the vendee or lessee, to purchase or lease from such vendor

gress passed the Clayton Act,¹⁸ which prohibited both anticompetitive tying and exclusive dealing in goods “whether patented or unpatented.”¹⁹ Congress accomplished this by amending the antitrust laws rather than the Patent Act—the only time Congress expressly changed the legality of a patent practice by amending the antitrust law. The language used in the Clayton Act, “condition . . . or understanding,” prohibited both ordinary contracts and license restraints.²⁰

Thus the first sale doctrine performed the very useful service of dividing the territory between federal patent infringement law, where the states could not interfere, and the licensing of patented “things,” in Walker’s terms, where state law governed.²¹ The Supreme Court had already observed this problem of federalism by 1859, when it held in *Chaffee v. Boston Belting Co.* that “[b]y a valid sale and purchase, the patented machine becomes the private individual property of the purchaser, and is no longer protected by the laws of the United States, but by the laws of the State in which it is situated.”²²

The First Circuit applied this principle the same year. The Goodyear process for using heat and pressure to make vulcanized rubber was a substantial technological innovation. In the *Goodyear v. Beverly Rubber* case, Charles Goodyear had licensed out his process, limiting its use to the manufacture of shoes.²³ The infringement defendant, who was not a licensee, was in the business of scavenging worn out shoes made with the process, grinding up the rubber and using a different process to make it commercially feasible for other uses. Quoting the above language from *Boston Belting*, the Massachusetts court applied the first sale doctrine, noting that the shoes made under Goodyear’s license had been sold to others and subsequently acquired by the defendant. As a result, defendants were no longer within the patent monopoly.²⁴ Four years later,

or lessor such component and constituent parts of said tool, implement, appliance or machine, as the vendee or lessee may thereafter require during the continuance of such patent right: provided, that nothing in this act shall be construed to prohibit the appointment of agents or sole agents to sell or lease machinery, tools, implements or appliances.

¹⁸ 15 U.S.C. § 14 (2012).

¹⁹ *Id.*

²⁰ *Id.*

²¹ Walker, *supra* note 8, at 144.

²² 63 U.S. (22 How.) 217, 223 (1859).

²³ 10 F. Cas. 638 (C.C.D. Mass. 1859) (No. 5,557).

²⁴ *Id.* at 641.

in *Bloomer v. Millinger*,²⁵ the Supreme Court adhered to its initial first sale decision,²⁶ again quoting the above-referenced *Boston Belting* language.

The same distinction was applied for the first time in a patent tying case in a First Circuit decision in 1865.²⁷ In *Aiken v. Manchester Print Works*, the licensee had purchased a patented knitting machine from the patentee, subject to a restriction requiring the licensee to use only the patentee's consumable needles.²⁸ The infringement claim arose when the licensee manufactured its own needles. The court again quoted this same language from *Boston Belting* and concluded that any relief the patentee might obtain should come from the "courts of the state, according to the laws of the state, and not in the federal courts, under the special jurisdiction conferred for the protection of patent rights."²⁹ That is, the function of the first sale doctrine was to reserve the power to control patent ties to the states.

A state court again applied the doctrine in an 1866 exclusive dealing case, where the court used the same language concerning the division between federal and state law.³⁰ Sewing machine inventors Elias Howe and Isaac Singer entered a license agreement with dealers requiring the dealers to pay a license fee for every sewing machine that they sold, whether or not it was the patentees' machine.³¹ In today's parlance, that is a form of exclusive dealing, whereby rivals are forced to incur higher costs because they must pay for access to the primary dealer.

Prior to the Progressive Era, the leading Supreme Court patent tying decision was *Morgan Envelope Co. v. Albany Perforated Wrapping Paper Co.* in 1894.³² The patentee sold its patented toilet paper dispenser

²⁵ 68 U.S. (1 Wall.) 340, 351 (1863) (citing *Boston Belting*, 63 U.S. (22 How.) at 223).

²⁶ *Bloomer v. McQuewan*, 55 U.S. (14 How.) 539, 550 (1852).

²⁷ *Aiken v. Manchester Print Works*, 1 F. Cas. 245, 246–47 (C.C.D.N.H. 1865) (No. 113). The first suggestion of a tying claim arose in another case which, like *Millinger*, involved the Woodward patents on a wood planing machine. See *Wilson v. Simpson*, 50 U.S. (9 How.) 109, 125–26 (1850) (finding that the purchaser took machine free of the patent monopoly and was thus entitled to replace its cutters and knives, notwithstanding license restriction requiring them to be purchased exclusively from seller).

²⁸ *Aiken*, 1 F. Cas. 245.

²⁹ *Id.* at 247.

³⁰ *Howe v. Wooldredge*, 94 Mass (12 Allen) 18, 23–24 (1866).

³¹ *Id.*

³² 152 U.S. 425 (1894); see also *Wagner Typewriter Co. v. F.S. Webster Co.*, 144 F. 405, 411–12 (C.C.S.D.N.Y. 1906) (applying same reasoning to tie of patented Underwood typewriters and unpatented typewriter ribbons); cf. *Goodyear Shoe Mach. Co. v. Jackson*, 112 F.

with a license restriction requiring purchasers to buy its toilet paper. A patent on the paper roll had been rejected for lack of novelty.³³ The court again quoted *Boston Belting* on the distinction between federal and state law. Once the patentee had sold the dispenser, the tying requirement could not be enforced by a federal patent infringement suit but must be evaluated under state law.³⁴

In all of these early cases, exhaustion doctrine served to distinguish state prerogatives governing “patented things” from federal law governing the patents themselves. For example, if the first sale doctrine had not been applied to patent ties, then the tying requirements could be enforced by an infringement or contributory infringement action in which federal patent policy was paramount. Such an application would have amounted to a per se declaration approving patent ties as a matter of federal law, free from state interference.

That is precisely what happened in the 1912 *Henry* decision,³⁵ just when both states and the federal government were developing heightened concerns about practices such as tying, exclusive dealing, and RPM. New York, the state where *Henry* arose, had already declared RPM unlawful under state antitrust law,³⁶ and the Supreme Judicial Court of Massachusetts had already upheld the constitutionality of a statute condemning patent ties.³⁷ By enforcing such restrictions through patent infringement suits, patentees would have foreclosed all inquiries into competitive harm, because the Patent Act itself never addressed such concerns,³⁸ and federal patent policy would have ridden roughshod over conflicting state policy about the use and sale of patented articles.

146, 150 (1st Cir. 1901) (finding permissible repair rather than reconstruction when purchasers of heavy duty sewing machines used for making shoes replaced the machines' worn out cams); *Morrin v. Robert White Eng'g Works*, 138 F. 68, 77 (C.C.E.D.N.Y. 1905) (holding that part replacement constituted a repair rather than reconstruction when consumption of the replaced part is an essential element of the device).

³³ See *Heaton-Peninsular Button-Fastener Co. v. Eureka Specialty Co.*, 77 F. 288, 298–99 (6th Cir. 1896).

³⁴ Id. at 299 (quoting *Boston Belting*, 63 U.S. (22 How.) at 223).

³⁵ *Henry*, 224 U.S. 1.

³⁶ *Straus v. Am. Publishers' Ass'n*, 69 N.E. 1107, 1109 (N.Y. 1904).

³⁷ *In re Op. of the Justices*, 81 N.E. 142, 147 (Mass. 1907); see supra note 17 and accompanying text.

³⁸ The Patent Act first addressed tying claims in 1988. See 35 U.S.C. § 271(d)(5) (1988) (providing that patent ties are lawful unless the patentee had market power in the market for the patented product).

The short-lived *Henry* decision³⁹ was an unusual case in which the Supreme Court did *not* apply exhaustion. The parties reasonably anticipated the result, however, because decision author Justice Lurton and Chief Justice Taft had sat on an earlier Sixth Circuit panel that applied precisely the same reasoning.⁴⁰ *Henry* permitted the patentee to bring a contributory infringement action against defendant Henry, who had sold a can of ink in knowing violation of the tying condition in the plaintiff's patent license.

Chief Justice White argued the federalism point in his *Henry* dissent:

[T]he ruling now made has a much wider scope than the mere interest of the parties to this record, since, in my opinion, the effect of that ruling is to destroy, in a very large measure, the judicial authority of the states by unwarrantedly extending the Federal judicial power. . . . [T]he gravity of the consequences which would ordinarily arise from such a result is greatly aggravated by the ruling now made, since that ruling not only vastly extends the Federal judicial power, as above stated, but as to all the innumerable subjects to which the ruling may be made to apply, makes it the duty of the courts of the United States to test the rights and obligations of the parties, not by the general law of the land, in accord with the conformity act, but by the provisions of the patent law, even although the subjects considered may not be within the embrace of that law, thus disregarding the state law, overthrowing, it may be, the settled public policy of the State, and injuriously affecting a multitude of persons.⁴¹

³⁹ *Henry*, 224 U.S. 1. *Henry* was expressly overruled soon after the Clayton Act was passed by *Motion Picture Patents Co. v. Universal Film Manufacturing Co.*, 243 U.S. 502, 518 (1917). As Duffy and Hynes point out, however, the Court's first sale analysis in *Henry* was substantially undermined by *Bauer & Cie v. O'Donnell*, 229 U.S. 1, 17–18 (1913) (holding that exhaustion doctrine precluded enforcement of an RPM provision). See Duffy & Hynes, *supra* note 1, at 23–24.

⁴⁰ *Heaton-Peninsular Button-Fastener Co. v. Eureka Specialty Co.*, 77 F. 288, 296 (6th Cir. 1896) (enforcing patent tie via infringement action).

⁴¹ *Henry*, 224 U.S. at 49–50 (White, C.J., dissenting). Chief Justice White's reference to the "conformity act" was undoubtedly referring to the Conformity Act of 1872, ch. 225, § 5, 17 Stat. 197 (codified as amended at Rev. Stat. § 914 (1878)), a pre-*Erie* statute requiring that pleading and practice in federal courts conform to the extent possible to the pleadings and practices in the courts of that state, and that common law remedies in the federal courts be made as similar as possible to the state court's own remedies. See *Erie R.R. Co. v. Tompkins*, 304 U.S. 64, 78 (1938) ("Except in matters governed by the Federal Constitution or by Acts of Congress, the law to be applied in any case is the law of the State.").

Duffy and Hynes read this passage as supporting their argument that the majority's refusal to apply the first sale doctrine would read patent law broadly to "*displace other law*."⁴² I read it to be much more specific than that. The dissenters' concern was that, absent exhaustion, federal patent law was in effect being used to displace *state* law in an area that had always been reserved to the states.

Eventually federal antitrust came to dominate the field of patent and antitrust law, limiting enforcement by both contract law and patent infringement suits. During this formative era, however, when state antitrust law often led the way in the formulation of licensing policy, the first sale doctrine served as a mechanism for preserving Walker's distinction between "patents" and "patented things," according the latter to the law of the states.⁴³

⁴² See Duffy & Hynes, *supra* note 1, at 23.

⁴³ Walker, *supra* note 8.